

ORIGINAL



0000074936

47

BEFORE THE ARIZONA CORPORATION COMMISSION

Arizona Corporation Commission

DOCKETED

JAN 7 2008

DOCKETED BY

COMMISSIONERS

MIKE GLEASON, Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE

IN THE MATTER OF THE REVIEW AND
POSSIBLE REVISION OF ARIZONA UNIVERSAL
SERVICE FUND RULES, ARTICLE 12 OF THE
ARIZONA ADMINISTRATIVE CODE.

Docket No. RT-00000H-97-0137

IN THE MATTER OF THE INVESTIGATION OF
THE COST OF TELECOMMUNICATIONS
ACCESS.

Docket No. T-00000D-00-0672

COMMENTS OF AT&T

Pursuant to the Procedural Order entered in these dockets dated November 28, 2007,
AT&T Communications of the Mountain States, Inc. and TCG Phoenix (collectively referred to
as "AT&T") file these comments on access charge reform and possible revisions to the Arizona
Universal Service Fund ("AUSF") Rules.

INTRODUCTION

The Commission has sought comment on a broad array of issues under two related
subjects: (i) access charge reform and (ii) universal service. AT&T agrees that the Commission
should consider those two subjects together. Access charge reform is long overdue because the
current access charges of some carriers still reflect levels of implicit subsidies that are
fundamentally inconsistent with today's telecommunications landscape. Universal service

GALLAGHER & KENNEDY, P.A.
2575 E. CAMELBACK ROAD
PHOENIX, ARIZONA 85016-9225
(602) 530-8000

RECEIVED

RECEIVED

1 programs, meanwhile, have been founded on the recognition that such implicit subsidies cannot
2 and should not be maintained in today's competitive marketplace.¹

3 It is also quite proper and, indeed, essential that the Commission consider access charge
4 reform and universal service now. The current access charge system creates large implicit
5 subsidies that inflate some carriers' intrastate switched access charges. To take a few examples:
6 Terminating intrastate access charges for one ICO are more than *18.4 cents per access minute*, or
7 *46 times* its 0.4 cent interstate charges, and *more than five times higher than Qwest's*
8 *corresponding intrastate charges*. For originating access, that ICO's tariffed intrastate rate is
9 10.4 cents, while its corresponding interstate rate is only 0.4 cents. Likewise, a second ICO has
10 intrastate terminating access charges approaching 5 cents per minute, but only about 2.5 cents
11 interstate. One CLEC has intrastate terminating access charges of over 4.2 cents per access
12 minute, while its corresponding interstate charges are less than half a penny. As a general
13 matter, these relationships hold true for virtually all of Arizona's ICOs and CLECs throughout
14 the State.

15 The high access rates promoted by the current system obviously distort Arizona
16 telecommunications prices. They make long distance prices higher than they should be for all
17 Arizonans, including consumers in the Phoenix and Tucson metropolitan areas, because long
18 distance rates are geographically averaged. The implicit subsidies hidden in inflated access
19 charges cause rates for some services (in particular, long distance service) to be over-priced,
20 while other rates (such as local exchange service in rural areas) remain below cost. As a result,
21 the pricing signals being given to Arizona customers are blurred, resulting in consumers shifting

22
23 ¹ The Commission recognized this link when it initially adopted the Competitive Telecommunications
24 Rules in 1995 (A.A.C. R14-2-1101, *et seq.*). It provided in those rules that an AUSF should be
established. R14-2-1113. The AUSF Rules (R14-2-1201, *et seq.*) were adopted the following year.

1 usage to services which may be less economically efficient (because those services are
2 subsidized) and causing telecommunications-dependent businesses to configure their services to
3 avoid being saddled with disproportionate subsidy obligations. In addition, high access charges
4 encourage some actors to exploit the system by engaging in arbitrage and traffic pumping
5 schemes. At bottom, the implicit cross-subsidies inherent in access rates in Arizona are a house
6 of cards that simply cannot and should not be maintained in today's telecommunications market.

7 The Federal Communications Commission ("FCC") has already implemented reforms
8 that have begun to eliminate implicit subsidies from interstate access rates. Several states (such
9 as New Mexico and Nebraska) have also implemented reforms to reduce intrastate access
10 charges to more reasonable and sustainable levels. In each state, the commission used interstate
11 access rates as a benchmark above which rates are presumed to be excessive, and generally these
12 states allowed carriers to recover the lost revenues through rate rebalancing and/or explicit
13 universal service subsidies. AT&T recommends that the Commission take the same approach
14 here by (i) requiring all local exchange carriers, using appropriate and streamlined rate
15 procedures, to lower their intrastate access rates to the level (and structure) of the corresponding
16 interstate access rate levels and (ii) allowing carriers to rebalance the revenue reductions with
17 increases to retail rates and, in certain cases, from AUSF funds. This approach represents a
18 straightforward step that can be implemented relatively easily and quickly. It will result in more
19 economically rational prices for wireline services.

20 Of course, the FCC is considering comprehensive reform for all forms of intercarrier
21 compensation on a national basis. But there is no sign that comprehensive reform will come any
22 time soon and in the absence of such national reform there is an urgent need to take action with
23 regard to intrastate switched access rates. The approach proposed by AT&T here represents a

1 measured, straightforward step that will make significant progress in correcting the most serious
2 defects of the present system. It is a step that the Commission can take relatively quickly,
3 without undue delay or lengthy proceedings.

4 Universal service reform represents the other side of the coin of access charge reform.
5 Universal service support is designed to replace the implicit subsidies of the past with explicit
6 subsidies for basic local telecommunications services where those subsidies are needed. The
7 funds for that support should come from contributions by customers of all service providers on
8 an equitable and non-discriminatory basis that mirrors the federal universal service contribution
9 methodology, because all consumers and all providers benefit from the expansion of the
10 telecommunications network. As detailed in Section II below, in addition to supporting explicit
11 recovery for portions of reduced intrastate switched access revenues not recovered through
12 reasonable rate increases, AT&T also supports AUSF support for carriers of last resort
13 ("COLRs") that serve high-cost areas, where there is a demonstrable need for such support to
14 maintain affordable basic service rates, to the extent such support is not already provided by the
15 federal universal service fund.

16 DISCUSSION

17 I. Access Charge Reform Questions

18 A. Background

19 Charges for switched access services generally refer to the price paid by interexchange
20 carriers ("IXCs") and other telecommunications service providers to a local exchange carrier
21 ("LEC") for the use of its network. It is the LEC that has the local loop and central office switch
22 that connects an end user to the rest of the PSTN. IXCs need access to this local exchange
23 infrastructure in order to originate intrastate and interstate long distance calls from customers

1 served by the LEC, and to complete long distance calls from their own customers to customers
2 served by the LEC.

3 Prior to 1996, local telephone service and local exchange carriers were regulated as
4 natural monopolies. Monopoly service providers were required to provide universal service to
5 all customers in their assigned territories. They were able to serve high-cost customers (e.g.,
6 customers in remote rural areas) through a system of "implicit subsidies," under which the rates
7 paid by some customers were overstated (i.e., in excess of the rates necessary to adequately
8 recover costs) in order to subsidize understated rates for other customers. Historically, the
9 intrastate access charges that rural LECs charged to IXC's were set above cost to provide implicit
10 price support for local exchange service.

11 As demonstrated by the table below, showing tariffed access rates, that system of implicit
12 subsidies is still embedded in the intrastate access charge structure for many LECs in Arizona.
13 Intrastate access fees in Arizona are much, much higher than the corresponding *interstate* fees,
14 even though carriers use the same facilities to originate and terminate both interstate and
15 intrastate calls.

Intrastate Access Tariff Rates

Company Name	Type	Orig Unit Cost	Term Unit Cost	Average Unit Cost
Qwest-AZ	ILEC	\$0.027	\$0.035	\$0.031
Qwest-Interstate	ILEC	\$0.003	\$0.003	\$0.003
Delta		\$0.024	\$0.032	\$0.028
Citizens-Intrastate	ICO	\$0.104	\$0.184	\$0.144
Citizens-Interstate	ICO	\$0.004	\$0.004	\$0.004
Delta		\$0.100	\$0.180	\$0.140
Valley-Intrastate	ICO	\$0.102	\$0.102	\$0.102
Valley-Interstate	ICO	\$0.026	\$0.026	\$0.026
Delta		\$0.076	\$0.076	\$0.076
Accipiter-Intrastate	ICO	\$0.035	\$0.049	\$0.042
Accipiter-Interstate	ICO	\$0.026	\$0.026	\$0.026
Delta		\$0.009	\$0.023	\$0.016
Cox Arizona-Intrastate	CLEC	\$0.033	\$0.042	\$0.037
Cox Arizona-Interstate	CLEC	\$0.003	\$0.003	\$0.003
Delta		\$0.029	\$0.039	\$0.034
Source/Notes:				
Rates shown above were obtained from Qwest and ICO access tariffs.				
Rates do not include direct trunk transport.				
Assumes 10 miles for mileage sensitive transport rates.				
Assumes 20% of the minutes are tandem routed and 80% are direct routed.				
The average unit cost was calculated by adding originating plus terminating cost and dividing by two.				

While such a system of cross-subsidies was sustainable in the protected monopoly market structure of the past, the influx of competitive alternatives in today's marketplace renders such approaches ineffective and unsustainable. There are several competitive alternatives to traditional switched long distance services (primarily alternatives like cable telephony, Voice over Internet Protocol ("VoIP") and wireless). Whenever an ILEC's end user chooses to use an alternative to make long distance calls, the ILEC's subsidy revenue stream (in the form of access

1 charges) may be reduced. The retail rates for these competitive alternatives do not necessarily
2 include the same implicit subsidies that long distance service providers are forced to support.

3 The implicit subsidies in switched access rates—and the economic reactions that they
4 trigger—are harming Arizona consumers and the Arizona telecommunications market. As the
5 market proves time and again, any effort to impose implicit subsidies on one class of customers
6 simply leads those customers to find ways to avoid paying the subsidies. Thus, in recent years,
7 ILECs have lost billions of minutes to services that are alternatives to traditional long distance, in
8 part because of the high access costs for switched access.

9 The sustainability of implicit subsidies is further threatened in cases where carriers
10 dispute which compensation mechanism should applied to a given call. For example, with
11 respect to VoIP traffic, certain VoIP providers have asserted that VoIP services are exempt from
12 access charges,² and through self-help measures attempt to have their calls treated as local calls.

13 The disparate regulatory treatment of calls for intercarrier compensation purposes has
14 also strained the reliability of implicit subsidies. For example, with respect to wireless, nearly all
15 of Arizona (including Phoenix, Tucson and Flagstaff) is encompassed by a single Metropolitan
16 Trading Area (“MTA”). Thus, under federal rules virtually all wireless calls that originate and
17 terminate within Arizona are exchanged over local interconnection arrangements and are treated
18 as local calls for intercarrier compensation purposes.

19 The current structure thus not only artificially overstates the ILECs’ toll rates, but also
20 jeopardizes the universal service that the old implicit subsidies were designed to support.

21
22 ² There is disagreement within the industry as to which compensation mechanism should apply to VoIP
23 traffic as the FCC has not provided clarification. Some carriers assert that such traffic is subject only to
24 reciprocal compensation charges while others assert that it is subject also to switched access charges. As
a result of this disagreement, compensation for VoIP traffic is in dispute, which further threatens the
sustainability of implicit subsidies contained in access charges.

1 Above-cost access charges were intended to subsidize the ILEC's local exchange service. But
2 high access charges may drive consumers to competitive alternatives that do *not* subsidize the
3 LEC with the same level of intrastate access charges. The flow of subsidies is thereby reduced
4 and eventually the LEC will be unable to sustain local service priced below market rates.

5 Market forces alone are not sufficient to remove implicit subsidies from intrastate access
6 charges. With respect to originating access, rate averaging prevents market forces from
7 operating to discipline switched access rates. IXCs are required by federal law to geographically
8 average interstate rates and, for all practical purposes, are forced to do the same with intrastate
9 rates. Thus, an IXC is unable to pass any unreasonably high originating switched access rates
10 back to the calling party, which means that consumers receive no market signals, in the form of
11 higher prices from IXCs subject to higher CLEC access rates, to switch to CLECs or ILECs who
12 charge lower access rates.

13 For terminating access, the LEC possesses the bottleneck network element which
14 prevents the operation of market forces. For example, if an IXC's customer seeks to make a toll
15 call to a party receiving local exchange service from a LEC, the LEC collects terminating access
16 from the IXC for use of the LEC's network to complete the toll call. The IXC carrying the call
17 has no alternative; the call must be delivered to the LEC whose customer is receiving the call.
18 As such, markets alone are incapable of disciplining intrastate access rates.

19 High switched access rates also engender arbitrage. Carriers that receive access charges
20 have an incentive to increase volumes. The recent, highly publicized "traffic pumping" schemes,
21 which are designed to drive massive volumes of traffic to adult chat lines and similar services
22 (such as free conference call offers) via rural LECs with high switched access rates, serve to
23
24

1 highlight the potential for abuse.³ Conversely, carriers that pay access charges have an incentive
2 to evade them. High switched access rates create an incentive for “buying” carriers to assert
3 claims that certain types of toll traffic are subject to reciprocal compensation rather than access
4 charges or to generate “phantom” traffic that is difficult or impossible to assign to a jurisdiction.
5 Reforms that bring switched access rates closer to cost will reduce the incentive for such abuse
6 and arbitrage.

7 At the federal level, the FCC has taken several steps to reduce interstate access charges.⁴
8 Several states have followed the FCC’s lead. In each state, the commission uses interstate access
9 rates as a benchmark for intrastate rates. This approach takes advantage of two facts: (i) the
10 FCC has already reduced the implicit subsidies in interstate rates and (ii) the cost of switching a
11 call, whether it is subject to intrastate or interstate access charges, is the same. These states have
12 also typically allowed carriers to recover the lost access revenues through rebalanced rates or
13 explicit universal service subsidies. To take a few examples:

- 14 • In New Mexico, pursuant to N.M. Admin Code § 17.11.10.8, the statewide average
15 switched access rate for originating and terminating intraLATA toll calls is to be reduced
16 effective January 1, 2008 to the level of interstate access rates (in effect as of January 1,
17 2006) for a state-wide average of only \$0.0183 per minute to originate or terminate an
18 in-state long distance call.⁵ Section 17.11.10.6 provides that the state’s universal service
19 fund is to “includ[e] the implementation of a specific, predictable and sufficient support
20 mechanism that reduces intrastate switched access charges to interstate switched access
21 charge levels *in a revenue-neutral manner* and ensures universal service in the state.”
- The Nebraska Public Service Commission also adopted parity with the interstate rate
structure as its goal. *Investigation into Intrastate Access Charge Reform*, Application
No. C-1628, 1999 WL 135116, *4 (Neb. P.S.C., Jan. 13, 1999). That commission
recognized that “[d]ue to the opening of ILEC markets to competition, this subsidization
practice [in intrastate access charges] is no longer desirable.” *Id.* at *2. The commission

22 ³ See *In re Establishing Just & Reasonable Rates for Local Exchange Carriers*, Notice of Proposed
Rulemaking, 22 F.C.C. Rcd. 17989 (2007).

23 ⁴ See response to Question 7 *infra*.

24 ⁵ The referenced per minute rate based on using the NECA ATS rate as a proxy for rural ILEC interstate
switched access.

1 further found that “[t]he lost support” resulting from reductions in intrastate access
2 charges “may, over a reasonable period of time, be replaced through increases in rates
3 and by state and federal universal service funds.” *Id.* Beginning in 1999, the Nebraska
commission implemented a multi-year reform, and the average rural ILEC rates in the
state are now approximately \$0.02 per minute.

- 4 • In Maine, all carriers are required to true-up their intrastate rates to interstate parity every
5 two years. 35-A M.R.S.A. § 7101-B (2005); ME ADC 65-407 Ch. 280, § 8(B) (“On or
6 before every two years . . . all local exchange carriers shall reestablish intrastate access
7 rates that are less than or equal to the interstate rates for that carrier”).⁶
- 8 • Likewise, Kansas requires that access fees charged by rural telephone companies be
9 reduced every two years until they reach parity with interstate fees. K.S.A. § 66-2005(c)
10 (“Subject to the commission’s approval, all local exchange carriers shall reduce intrastate
11 access charges to interstate levels as provided herein. . . . The commission is authorized
12 to rebalance local residential and business service rates to offset the intrastate access and
13 toll charge reductions.”).
- 14 • In New Hampshire, although state law does not mandate intrastate access rate reductions
15 to interstate levels, “as soon as possible after each significant decrease of interstate access
16 charges by the federal government,” the commission is to “consider corresponding
17 reductions in intrastate access charges, taking into account both the disadvantages to
18 customers of intrastate access charges that exceed interstate access charges and the
19 disadvantages to customers of increases in charges for basic service.” N.H. Rev. Stat.
20 § 378:17-a(III). The commission is also to consider “reducing intrastate access charges
21 and increasing basic monthly service charges” for LECs whose intrastate access charges
22 are above the state median and whose basic monthly service charges are below the state
median for carriers with similar numbers of telephones. *Id.*
- 23 • In Indiana, if a provider’s rates and charges for intrastate switched access service are at
24 issue in a proceeding before the commission or “included in interconnection agreement or
a statement of terms and conditions the commission is authorized to review or approve,”
“the commission shall consider the provider’s rates and charges for intrastate . . . access
service to be just and reasonable if the intrastate rates and charges mirror the provider’s

⁶ In Maine, prior to the initial receipt of support from the Universal Service Fund, a rural LEC must
“establish intrastate access rates that meet the requirements of 35-A M.R.S.A. § 7101-B and Chapter 280,
§ 8 of the Commission’s Rules.” ME ADC 65-407 Ch. 288, § 3.

1 interstate rates and charges.” IC 8-1-2.6-1.5.⁷ The Indiana commission created the
2 Indiana Universal Service Fund as a revenue replacement fund to address revenue lost by
3 a carrier as a result of intrastate access reductions caused by mandatory mirroring of
interstate rates, the docket included a minimum local rate as part of the rate rebalancing.
4 *See Re Universal Service Reform*, Cause No. 42144, 2004 WL 1170315 (Ind. Util. Reg.
Comm’n, Mar. 17, 2004).

5 AT&T proposes that this Commission take the same straightforward approach here. The
6 Commission should establish procedures to require all LECs, incumbents and competitors alike,
7 to reduce intrastate switched access charges to the level of the corresponding interstate rates as
8 detailed herein. In addition, the intrastate rate structure for all access charges should mirror the
9 structure at the federal level. Carriers should then be given the opportunity to recover those
10 revenue reductions through increased retail rates and, in certain circumstances, the Arizona
11 Universal Service Fund (as described in Section II below).

12 **B. Response to Staff Questions**

13 1. *Do you believe that the Commission ought to restructure access charges? Please
14 explain your response.*

15 Yes. As detailed above, intrastate switched access charges in much of Arizona are well
16 above the corresponding charges at the interstate level and in other states. Such high charges

17 ⁷ In the same vein, other states have adopted a parity requirement for carriers electing price or alternative
18 regulation. *See* I.C.A. § 476.97 (under Iowa law, carriers submitting a plan for price regulation must
19 include a proposal “for reducing the local exchange carrier’s average intrastate access service rates to the
20 local exchange carrier’s average interstate access service rates”; the time frame allowed for the reduction
21 depends on the number of access lines); W.S.A. § 196.196 (under Wisconsin law, the intrastate access
22 rates for utilities electing price regulation may not exceed their interstate rates for similar services; the
23 time frame for accomplishing parity depends on the number of access lines in use); Ga. Code Ann.
24 § 46-5-166 (under Georgia law, the switched access rates of LECs electing alternative regulation shall be
no higher than for interstate access; the time frame for implementing the parity requirement depends on
the number of access lines); NV ADC § 704.6848 (under Nevada law, as a condition of entering a plan of
alternative regulation, the provider must “adjust its rates for intrastate switched access . . . to the extent
that such elements correspond to the rates for interstate access, so that those rates will be in parity with its
rates for interstate switched access at the time of the entry into the plan”). *See also* NV ADV
§ 704.68048 (under Nevada law, in order for a small provider of last resort to qualify for universal service
funds, “[i]ts rates for interstate and intrastate switched access must be in parity, or the small provider must
agree to carry out a plan approved by the Commission designed to achieve parity for those rates within
the time specified by the Commission”).

1 reflect anachronistic implicit subsidies, which are harmful in today's competitive environment.
2 In comments filed with the FCC, this Commission has recognized the need for reform in the area
3 of intercarrier compensation, including the existing switched access structure.⁸ AT&T
4 respectfully submits that it is necessary and appropriate for this Commission to act by taking a
5 measured step as proposed herein, especially in the absence of significant progress on
6 comprehensive reform at the FCC.

7 2. *What recommendation to the Commission would you make regarding how*
8 *intrastate access charges should be reformed?*

9 The stability of the current system of rates and support for basic voice services in high-
10 cost areas depends on addressing the implicit subsidies in intrastate switched access charges.
11 The Commission should reduce the implicit subsidies currently imbedded in intrastate switched
12 access charges and replace them as appropriate with explicit recovery mechanisms. Several
13 states have reformed access charges by requiring ILECs and CLECs to lower their intrastate
14 access rates to the level of interstate access rates. AT&T proposes that this Commission adopt
15 the same approach and that it also require ILECs and CLECs to mirror interstate rate structures
16 as detailed herein. Carriers should have the opportunity to recover the resulting reductions in
17 access revenues through increases to retail rates. For ILECs that have COLR obligations,
18 revenue recovery may include an intrastate access replacement universal service funding
19 mechanism for their rural and high-cost areas, as is further discussed in Section II below. To
20 maintain access rate uniformity, the Commission should require that future changes in a carrier's
21 interstate access rates be reflected in the same carrier's intrastate rates.
22

23 ⁸ Reply Comments of the Arizona Corporation Commission, *In the Matter of Developing a Unified Intercarrier*
24 *Compensation Regime*, CC Docket 01-92, p. 1.

1 3. *Would you recommend the Commission address both switched and special access*
2 *in an access charge reform proceeding? If your response is yes, please explain.*

3 No. The Commission should focus on intrastate switched access with the objective of
4 reducing implicit subsidies, and offsetting the resulting loss of revenues through increased
5 flexibility in retail rates, increases in state universal service funding, and other support
6 mechanisms as appropriate. This will result in more economically rational prices for switched
7 telephone services.

8 Special access services, meanwhile, comprise a very different set of services that are
9 subject to a different set of market forces. For example, as described above a switched-access
10 IXC does not control the numbers that its customer will dial. It has little choice but to deliver its
11 customer's call to the number dialed and to incur whatever terminating access charges apply. By
12 contrast, a special access facility connects two points that are defined by the buyer up front.
13 Given the controls of the market, there is no need to address special access services here and any
14 attempt to do so would needlessly complicate and delay the implementation of urgently needed
15 reforms in the switched access arena.

16 4. *What is your current recommendation to the Commission on how access charges*
17 *should be reformed?*

18 As AT&T discussed in Section I.A above, and in response to Questions 1 and 2, intrastate
19 switched access charges should be reduced to the level of the corresponding interstate rates as
20 detailed herein.

21 5. *Please update your response to the questions and issues contained in the 12-3-01*
22 *Procedural Order in Docket No. T-00000A-00-0672 to the extent you feel they*
23 *should be updated.*

24 The essence of AT&T's comments filed in Docket No. T-00000A-00-0672 is consistent
25 with the recommendations offered here. To take the leading example, AT&T previously

1 recommended that intrastate switched access rates should mirror interstate switched access rates,
2 and that the existing ILEC switched access rates should be utilized as a cap. Those
3 recommendations are consistent with AT&T's present proposal to reduce intrastate switched
4 access rates to the level of their interstate counterparts. To the extent that any elements of
5 AT&T's previous comments are inconsistent with any of AT&T's current proposals, AT&T's
6 current comments should control.

7 6. *How would the FCC's proceeding to reform intercarrier compensation affect the*
8 *ACC's actions to reform intrastate access charges?*

9 Since issuing its pending intercarrier compensation proceeding found at CC Docket
10 No. 01-92 in 2001,⁹ the FCC has yet to adopt comprehensive intercarrier compensation reform.
11 Although AT&T is steadfast in its view that the FCC and/or Congress should implement
12 intercarrier compensation reform as quickly as possible, and that the Missoula Plan is the
13 appropriate framework for doing so, at this juncture there is nothing to indicate that the FCC or
14 Congress intends to act any time soon. Indeed, given the upcoming federal elections, the issues
15 that are already on the FCC's agenda, and the complexities of crafting comprehensive national
16 solutions to these issues, it is unlikely that the FCC or Congress will issue meaningful reforms in
17 the near term.

18 The lack of progress on comprehensive reform at the national level provides an
19 opportunity—and, in fact, a pressing need—for the states to take a step and act on access and
20 universal service reform at the intrastate level. The Commission's comments opposing the
21 Missoula Plan make clear that this Commission "recognizes that reform is necessary in this
22 area," and also acknowledges that "intrastate access charges and . . . reciprocal compensation

23 ⁹ *In re Developing a Unified Intercarrier Compensation Regime*, CC Docket No. 01-92, FCC 05-33,
24 Further Notice of Proposed Rulemaking (released March 3, 2005)("FNPRM").

1 rates are areas within the jurisdiction of State commissions.”¹⁰ Several states have also
2 implemented access charge reforms and this Commission should do the same.

3 7. *Do you believe that the carrier common line switched access charges ought to*
4 *exist? Please provide your rationale for your position on this matter.*

5 No. Regulators at the state and federal levels have recognized the need to eliminate the
6 carrier common line (“CCL”) switched access charge. By way of its CALLS¹¹, MAG¹² and
7 CLEC Access¹³ orders, the FCC acknowledged the subsidies inherent in the CCL, the CCL’s
8 detrimental effect on competition, and the incompatibility of the CCL with the competitive
9 marketplace and with the requirement for explicit universal service support.

10 8. *Do you think that the notion of implicit subsidies ought to be a component of any*
11 *analysis that the Commission conducts?*

12 Absolutely. The driving need for access reform in this State is the fact that implicit
13 subsidies continue to be included within the intrastate switched access charge structure. Under
14 its CALLS, MAG and CLEC Access orders, the FCC sought to minimize the subsidies inherent
15 in interstate switched access. The difference that now exists between intrastate and interstate
16 switched access charges (i.e., level and structure) is attributable to the presence of implicit
17 subsidies. The Commission should take a measured step toward elimination of implicit subsidies

18 ¹⁰ *Id.*

19 ¹¹ *Access Charge Reform, Price Cap Performance Review for Local Exchange Carriers*, CC Docket
20 Nos. 96-262 and 94-1, Sixth Report and Order, *Low-Volume Long-Distance Users*, CC Docket
21 No. 99-249, Report and Order, *Federal-State Join Board on Universal Service*, CC Docket 96-45,
22 Eleventh Report and Order, 15 FCC Rcd. 1292, 12965 (“CALLS Order”).

23 ¹² *Multi-Association (“MAG”) Plan for Regulation of Interstate Services of Non-Price Incumbent Local*
24 *Exchange Carriers and Interexchange Carriers*, CC Docket No. 00-256, Second Report and Order and
Further Notice of Proposed Rulemaking, *Federal-State Join Board of Universal Service*, CC Docket
No. 96-25, Fifteenth Report and Order, *Access Charge Reform for Incumbent Local Exchange Carriers*
Subject to Rate-of-Return Regulation, CC Docket No. 98-77, Report and Order, *Prescribing the*
Authorized Rate of Return From Interstate Services of Local Exchange Carriers, CC Docket No. 98-166,
Report and Order, 16 FCC Rcd. 19613 (“MAG Order”).

¹³ *In re Access Charge Reform and Reform of Charges Imposed by Competitive Local Exchange Carriers*,
Seventh Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-262 (“CLEC
Access Order”).

1 at the intrastate level (just as the FCC has done at the interstate level and as several other states
2 have done) by requiring LECs' intrastate switched access rates to mirror their interstate access
3 rates as detailed herein.

4 9. *Do you believe that the AUSF ought to pick up any revenue reduction that may*
5 *occur as a result of the reform of access charges? Please provide the rationale*
6 *for your response.*

7 The Commission should continue to preserve universal service in rural and high-cost
8 areas, and to that end it should consider the use of explicit recovery mechanisms to replace the
9 elimination of implicit subsidies from intrastate switched access charges. *See* Section II below.
10 Carriers should have the opportunity to recover revenue reductions first through flexibility in
11 retail rates before AUSF support is considered. For example, a maximum rate could be
12 authorized with "headroom" to adjust for demonstrated revenue reductions. For ILECs
13 performing COLR functions, it may also be appropriate to consider high-cost support where such
14 support is needed to maintain affordable rates for basic service in rural and high-cost areas. As
15 necessary, the Commission may need to modify its existing rules and/or adopt different
16 adjustable rate structures to permit the pricing flexibility necessary to accommodate the revenue
17 rebalancing.

18 10. *If you believe that the AUSF ought to pick up any revenue reduction that may*
19 *occur as a result of the reform of access charges, what parameters would you*
20 *implement to determine what amount ought to be picked up by the AUSF?*

21 In lowering price-regulated ILECs' intrastate switched access rates to interstate levels,
22 ILECs should first be allowed to make reasonable increases in their basic local service rates to an
23 appropriate rate benchmark. Portions of the access reductions which are not recovered through
24 such rate increases should be explicitly recovered through the AUSF for carriers that have COLR
obligations.

11. *How would you quantify the reductions? Please explain your response to include items such as whether the AUSF amount would be based on current year switched access minutes, on current year access revenues, historical year access minutes, historical year access revenues, etc.*

The Commission should establish a base-year period that predates a Commission order, such as 2007. Carriers would use their base-period demand and revenue to determine how much intrastate switched access revenue would need to be recovered. To illustrate, if the carrier's intrastate terminating switched access rates were reduced by 10 cents per minute, and it had 50,000 terminating minutes in the base year, the revenue to be replaced would be \$5,000. *See also* Section II.B, Question 12.

12. *Provide an estimate of the effect on access revenues for your company if access charges are reformed in the manner that you recommend to the Commission.*

AT&T is prepared to provide the Commission with the proprietary information it would need to make judgments about access rate reform and revenue rebalancing. However, such information is highly sensitive and must be protected from AT&T's competitors. To permit all carriers to make meaningful disclosures, the Commission should first take the following steps:

- determine which carriers should provide the requested information;
- enter a protective order to cover competitively sensitive information; and
- provide clear direction to carriers regarding the source and compilation of data, so that each carrier provides comparable information that will allow for “apples-to-apples” analysis.

13. *For companies that provide access service, please provide the dollar amount of revenues from intrastate switched access charges that you received by rate element, by month, for the period July 1, 2006 through June 30, 2007.*

AT&T is prepared to provide the Commission with this information. However, the information is highly sensitive and proprietary. To permit all carriers to make meaningful

disclosures, the Commission should first take the steps outlined in response to Question 12 above.

14. *For companies that purchase access service, please provide the dollar amount of the payments for switched access charges that you made (by company, rate element, and by month) for the period July 1, 2006 through June 30, 2006.*

AT&T is prepared to provide the Commission with this information. However, the information is highly sensitive and proprietary. To permit all carriers to make meaningful disclosures, the Commission should first take the steps outlined in response to Question 12 above.

15. *Should additional considerations be taken into account when restructuring and/or setting access charges for small rural carriers? Please explain your response.*

Yes. Small rural carriers serve high-cost areas and often obtain a greater share of their revenue from access charges than larger or urban carriers. Therefore, access reform can have a greater impact on such carriers. To the extent that data shows this effect, the Commission may make certain judgments regarding:

(1) the amount of access revenue that should be rebalanced into retail rates versus an access replacement, or high-cost, AUSF mechanism; and

(2) if a transition period is appropriate, whether the duration of a transition period should be prolonged for small rural carriers.

16. *Please comment on any other issues you believe may be relevant to the Commission's examination of intrastate access charges.*

Neither access reform nor universal service reform can be accomplished without the other. The historical and natural linkages of these two areas (and their relation to legacy subsidies) must be addressed in a coordinated and comprehensive fashion.

1 17. *Are there other issues besides the rate restructuring and costing issues raised*
2 *herein that should be addressed by the Commission in this Docket?*

3 It is possible that other issues may be raised by other parties in their comments or may
4 arise as new market or regulatory developments occur. AT&T may address other issues
5 interrelated to access rate and AUSF reform as they arise.

6 18. *Are there other State proceedings and/or decisions that you would recommend the*
7 *Commission examine in this docket? Please attach any relevant State commission*
8 *decisions to your comments.*

9 As previously mentioned, the FCC's CALLS, MAG and CLEC Access orders are useful
10 resources in understanding the need for and the path toward access reform. In addition, several
11 other states have used interstate access rates as a cap on intrastate rates. The applicable state
12 rules and statutes are referenced in Section I.A above.

13 19. *One of the stated objectives of the Qwest Price Cap Plan was to achieve parity*
14 *between interstate and intrastate access charges. Is this something that should be*
15 *looked at by the Commission in this proceeding?*

16 Definitely. As previously discussed herein, AT&T proposes that intrastate switched
17 access charges be lowered to mirror interstate access charges in terms of level and structure as
18 detailed herein. As Qwest is in the midst of a three-year access rate reform program, the
19 Commission should add that, at the earliest appropriate time, Qwest's intrastate switched access
20 charges should be further reduced to interstate levels. At that time, Qwest should be given the
21 pricing flexibility that will allow it to recover access revenue reductions. Only then will all
22 Arizona LECs operate on the same level playing field for access services.

23 20. *Parties who desire that switched access charges be reformed often state that*
24 *switched access charges in general, and the CCL rate element in particular,*
 contain implicit subsidies. Do you agree with this statement?

 Yes, as discussed in the Background to this section, and in response to Questions 1 and 7.

21. *Do you believe that the Commission should quantify implicit subsidies:*

a) *At all?*

No. There is no need for this Commission to engage in a detailed analysis or ratemaking to quantify the amount of implicit subsidies contained in current intrastate switched access rates. Such an analysis would be extremely difficult, time-consuming, costly and would unduly delay the implementation of reforms that are urgently needed now. The Commission should instead take the straightforward approach of following the actions already taken by the FCC to reduce implicit subsidies, by lowering all LEC intrastate switched access rates to interstate levels and requiring that intrastate switched access rates be structured in the same manner as interstate access rates as detailed herein. LECs utilize the same network functions in the provision of interstate and intrastate switched access services. Any interstate and intrastate rate differences are unjustified and harmful to the Arizona telecommunications market.

b) *As part of this proceeding?*

No. See response to part "a."

c) *As part of proceedings that address each carrier individually?*

No. *See* answer to part “a.”

22. *If you believe that the Commission should quantify implicit subsidies, what is the appropriate cost standard to be used to determine whether access charges are free of implicit subsidies?*

As stated in response to Question 21, AT&T does not believe it necessary or desirable for the Commission to conduct laborious and time-consuming cost analysis to attempt to determine the amount of implicit subsidies. Instead, as a measured step in intercarrier compensation reform, the Commission need only reduce intrastate switched access rates to the corresponding interstate rate levels as detailed herein.

1 23. *What issues do you believe should be addressed in a proceeding to determine*
2 *whether and to what extent intrastate access charges ought to be reformed?*

3 The issues discussed herein should serve as the starting point for intrastate access reform.

4 AT&T may address and/or recommend new issues as they are identified.

5 24. *Do you believe that there is a difference in the costs of providing interstate*
6 *switched access service versus intrastate-switched access service? In your*
7 *response, please include a description of how costs are defined in your response*
8 *and how those costs relate to costs allocated to the intrastate jurisdiction under*
9 *the FCC's current rules.*

10 No. Arizona LECs utilize the same network functions in the provision of interstate and
11 intrastate access services. Any interstate and intrastate rate differences are unjustified and
12 harmful to the competitive Arizona telecommunications market.

13 25. *Should the Commission address CLEC access charges as part of this Docket?*

14 Yes, as stated in response to Question 1 above, the Commission should reform access
15 charges for all LECs in Arizona. With respect to CLECs, high access charges constitute an
16 exorbitant subsidy flowing from the Arizona toll market to individual CLECs. These CLECs are
17 using high access charges to shift costs onto their competitors (both ILECs and IXC's). And as
18 discussed in Section I.A above, market forces alone are not sufficient to discipline such charges.

19 **II. Universal Service Issues**

20 **A. Background**

21 As noted above, historically universal service was funded by various implicit subsidies
22 embedded in the rates of the local exchange carrier. Implicit subsidies were previously
23 sustainable because a carrier could charge some consumers (such as urban business customers)
24 rates for local exchange and exchange access service that significantly exceeded the cost of
25 providing service and then use the rates paid by those customers to implicitly subsidize service to

1 others. But, in today's competitive markets, implicit subsidies can no longer be sustained. A
2 carrier that attempts to charge rates significantly above cost to one class of customers will lose
3 many of those customers to a competitor, because rational new competitors can target service to
4 more profitable customers without having to build into their rates the types of cross-subsidies
5 that have been required of incumbent carriers that serve all customers. Such price competition is
6 beneficial to customers, but also means that competitors' entry into the lowest cost, highest profit
7 market segments will dismantle the pillars of implicit subsidies (high access charges, high prices
8 for business services, and the averaging of rates over broad geographic areas) resulting in a
9 destabilized universal service funding base.

10 Universal service fund ("USF") support mechanisms are thus founded on the recognition
11 that while universal service remains a desirable public policy, implicit subsidies are no longer a
12 sustainable way to achieve that policy in today's hyper-competitive telecommunications markets.
13 Thus, in today's competitive environment, explicit support mechanisms, funded in an equitable
14 and nondiscriminatory manner by *all* providers and *all* customers, are necessary to replace the
15 loss of implicit subsidies and allow for the continuation of affordable and reasonable priced
16 universal service.

17 Often, when asked to describe what a Universal Service fund should be, a respondent lists
18 the same series of adjectives, such as "competitively neutral," "explicit," "cost-based" and
19 "revenue neutral." The differences lie in how to properly apply those broad policy goals in
20 practice. AT&T examines those issues, and Staff's questions, under the following general
21 subjects: (i) what should be funded, (ii) who should receive USF support and (iii) where the
22 funds should come from.

23 1. What Is Funded

1 The threshold question is to decide what the Fund should support. As discussed above,
2 the AUSF should be designed to explicitly recover portions of intrastate access rate rebalancing
3 not recovered through reasonable retail rate increases. AT&T also supports utilizing the AUSF
4 to support providers serving as carriers of last resort in high-cost areas where such support is
5 needed to maintain affordable rates for basic service.

6 Under this latter "high-cost support" approach, a carrier's support should be determined
7 by computing its revenue requirement whereby the carrier would recover the cost of plant
8 extension or build-out to unserved areas over the life of the assets. Thereafter, each year, for
9 each supported carrier, the carrier's support would be determined by (i) the carrier's revenue
10 requirement as developed by a cost model; (ii) the amount of federal universal service high-cost
11 support the carrier received (if any); and (iii) the revenues attributable to the customer through
12 the carrier's retail rates as defined by the high-cost benchmark. The carrier would receive in
13 AUSF support the difference between the carrier's revenue requirement on the one hand and
14 funds received in federal USF high-cost support plus retail revenues on the other. The process
15 would be similar in many ways to the concept proposed by ALECA.

16 In restructuring the AUSF, the Commission should ensure that carriers receiving AUSF
17 funding do not receive duplicated support for the same costs or facilities from the federal USF.
18 AT&T's proposed high-cost distribution methodology addresses this issue.

19
20 **2. High-Cost Support Should Be Provided Only to Carriers of Last
Resort**

21 To the extent that the AUSF is also used to provide high-cost support, such support
22 should be limited to carriers meeting a specific set of criteria, including a requirement that the
23 carrier accept the obligation to serve as a COLR: that is, the requirement to be ready and able to

1 provide a specified level of basic service to all customers in its designated area.¹⁴ Carriers
2 should be free to use alternative technologies to meet their COLR obligation, so long as the
3 technology provided the required minimum level of service. The basic level of service should
4 generally mirror the federal requirements found in 47 C.F.R. § 54.101(a)(1-9). This level of
5 service would include, among other things: (i) voice grade access to the public switched
6 network, (ii) local usage, (iii) access to emergency services, (iv) access to operator services and
7 (v) access to interexchange services. COLRs should also be required to provide Lifeline
8 (discounted rate) service to customers having low incomes.

9 It is critical that cost support be limited to COLRs. Universal service is about serving
10 customers that are not profitable (because the cost of providing service would exceed an
11 affordable rate) and such customers would not receive service absent some support. A carrier
12 that does not serve as a COLR will simply pick and choose those customers that it deems
13 profitable and ignore those customers that it finds unprofitable. Providing support to those
14 carriers results in less real public benefit (because non-COLR carriers will still not extend service
15 to the highest-cost, unprofitable customers where support is needed most) and more windfalls
16 (where the non-COLR receives a subsidy for serving a customer it would have profitably served
17 anyway). Further, the carrier that does undertake the COLR obligation is disadvantaged if
18 subsidies also go to competing carriers that serve only profitable customers.

19
20
21
22
23 ¹⁴ On the other hand, to the extent the AUSF is structured simply to replace the implicit subsidies that are
24 removed from access revenues, all ILECs that reduce their access charges as a result of access reform
could technically be eligible for AUSF support.

1 **3. Arizona USF Funding Should Be as Broad-Based as Possible, Should**
2 **Be Competitively Neutral, and Over the Longer Term Should Mirror**
3 **Any Future Changes to the Federal USF Contribution Methodology.**

3 The funds to be used for universal service support should come from *all*
4 telecommunications providers and customers, on an equitable, non-discriminatory and
5 competitively neutral basis. Federal law mandates that “[e]very telecommunications carrier that
6 provides intrastate telecommunications services shall contribute, on an equitable and
7 nondiscriminatory basis” to the preservation and advancement of universal service. 47 U.S.C.
8 § 254(f). As a policy matter, all providers and all consumers benefit from expanding the reach of
9 the public telecommunications network, so all providers and all consumers should bear their fair
10 share of the cost of maintaining such service throughout Arizona.

11 The existing AUSF contribution methodology may impose disproportionate burdens on
12 certain categories of service providers. Currently, the AUSF rules specify that one-half of AUSF
13 funding is to be borne by “Category 1” providers (largely local exchange carriers and wireless
14 carriers), on the basis of access lines and interconnecting trunks, respectively, and one-half of
15 AUSF funding is to be borne by “Category 2” service providers, i.e., providers of intrastate toll
16 service (or other service providers as permitted under R14-2-1204(B)(3), on the basis of
17 intrastate toll revenues.¹⁵ Not only does a different contribution methodology apply depending
18 on the type of service provider and service, but perhaps more importantly, the 50-50 allocation of
19 AUSF funding responsibility may bear no relationship to the providers’ level of activities in
20 Arizona relative to one another, if such activities were uniformly measured.

21 As a general matter, AT&T believes that the contribution methodology employed for the
22 AUSF (and all state USFs) should mirror that of the federal USF. Consistency between federal

23 _____
24 ¹⁵ See R14-2-1204.

1 and state funds facilitates carrier administration and compliance within the confines of the
2 carriers' system limitations. Carrier federal USF contributions are currently based upon a
3 percentage of interstate/international retail (end user) telecommunications revenues. However,
4 changes to the federal USF contribution methodology have been under consideration for some
5 time; specifically to move to a numbers- and connections-based contribution methodology.
6 AT&T supports such a change. Therefore, if in the future the FCC adopts such a contribution
7 methodology, AT&T recommends that the Commission review the AUSF contribution
8 methodology to mirror any change to the FCC's new contribution methodology, and allow a
9 reasonable transition period to allow carriers to implement such a change. Even before the FCC
10 acts, however, the Commission should consider implementing a more equitable contribution
11 methodology for the AUSF. To that end, AT&T is collecting more data and anticipates
12 providing a more refined recommendation for such a methodology in the next round of
13 comments.

14 **B. Answers to Staff Questions**

15 1. *What should the fund look like?*

16 To the extent that the AUSF provides high-cost support, the AUSF should most
17 appropriately provide support for costs, primarily loop and switching costs, to COLRs to allow
18 for the provision of basic service at affordable rates in high-cost areas. As described above,
19 high-cost support should be available only to carriers that undertake COLR obligations. For
20 non-rural carriers, the calculation of costs (to determine which areas are high-cost areas, and to
21 determine the amount of support necessary to compensate the COLR) should be done at the wire
22 center level (or a smaller geographic area). Costs vary by geographic area, and if costs are
23 calculated over larger regions, some high-cost areas might be missed because they are "averaged
24

out” by lower-cost areas in the same region. The calculation of costs for an efficient carrier could be linked to the FCC’s Synthesis Model or to the output of a state specific model. For rural carriers, support should be linked to the carrier’s annual NECA loop cost filing and possibly USAC Local Switching Support data. The AUSF support calculation should also account for federal USF high-cost support payments received by a carrier to avoid duplication of support: in essence, the AUSF should support that portion of federal USF costs above the federal cost benchmark, or state established benchmark, that is not already supported at the federal level.

2. *What revenues should be assessed?*

See Section II.A.3 above regarding the AUSF funding methodology.

3. *What should the AUSF reporting requirements be?*

All contributors to the AUSF should be required to submit and/or maintain for audit purposes sufficient information to verify that their contributions were correctly calculated. All providers that receive support should be required to submit and/or maintain for audit purposes sufficient data to calculate the support due and to ensure that the amounts paid to them were correct: for example, the number of customers served in high-cost areas multiplied by the applicable support amounts for those areas. Carriers may also need to report cost information if additional information is required beyond that available from NECA and USAC. In addition, if the AUSF is structured to serve as an access revenue replacement mechanism, carriers would need to provide information on the change in their intrastate access rates and their “base period” intrastate access minutes.

1 4. *What should the rules be for companies serving high-cost areas?*

2 It is unclear what "rules" are referenced by this question. To the extent the Commission
3 is seeking information as to the rules for receiving support, AT&T proposes that support be
4 limited to eligible telecommunications carriers that undertake the COLR obligation in the
5 specified area. Further, the carriers should provide the required minimum level of basic service
6 as determined by the Commission.

7 5. *Should all carriers be treated the same regardless of service area or technology*
8 *used?*

9 Generally speaking, yes. However, there should be minimum eligibility thresholds for
10 receiving AUSF high-cost support. First, the carrier should provide the required minimum level
11 of service as defined by the Commission, regardless of what technology it uses to provide that
12 service. Second, the carrier should be required to undertake the obligation of being a COLR in
13 an area or areas designated as high-cost by the adopted cost model or methodology.

14 6. *What revisions to the existing AUSF rules should be made?*

15 The Commission should make revisions to the existing AUSF rules to clearly set forth the
16 support structure described above. In particular, the Commission should adopt rules specifying
17 (i) the method for determining the appropriate surcharge, (ii) the method for determining which
18 areas are high-cost areas and for calculating the monthly support amounts and (iii) the
19 requirements for carriers to qualify for support (i.e., the required minimum level of service to be
20 provided, and the COLR obligation).

21 7. *Should the fund allow upfront recovery of construction costs?*

22 No. To the extent the Commission decides to use the AUSF as a high-cost support
23 mechanism, the recovery of construction costs (particularly loop costs) should be based on a
24

1 determination of costs and should account for costs recovered from the federal USF High Cost
2 Loop Fund, Safety Net Fund and Interstate Common Line Support. Support payments should be
3 paid monthly on a per-line basis. It is important to account for the time lag built into the federal
4 cost recovery mechanism. If AUSF support is paid up front, the Commission would be unable to
5 deduct federal USF support (which is paid after the fact), so the carrier would then receive a
6 double recovery when it receives its federal support. The coordination of benefits is important to
7 avoid double recovery of the costs by a carrier.

8 8. *Should a company be required to meet a set of criteria before they are allowed to*
9 *obtain AUSF revenues to compensate it for reductions in access revenues*
resulting from access charge reform?

10 Yes. See discussion in response to Questions 4 and 5 above.

11 9. *Should AUSF funding be available to competitive eligible telecommunications*
12 *carriers?*

13 For intrastate access reform purposes, AUSF support should not be necessary for a
14 competitive eligible telecommunications carrier (to the extent it experiences a decrease in access
15 revenue), given that competitive carriers have pricing flexibility that incumbents do not have.

16 To the extent that the AUSF also provides high-cost area support, support should be
17 available only to eligible carriers that can provide the required minimum level of service and that
18 undertake the obligation of being a COLR. In any given high-cost area, however, there should
19 be only one COLR.

20 10. *Should AUSF funding be provided to companies that are not certified as eligible*
telecommunications carriers?

21 No. High-cost support should be limited to those eligible telecommunications carriers
22 that undertake the obligation to be a COLR. In addition, the Commission may apply other
23 criteria or requirements for eligible carriers. In the case of AUSF support to offset intrastate

1 access charge reductions, support would technically be available to all carriers reducing their
2 rates to the extent they are not able to raise their basic service rates to offset the intrastate access
3 reductions; however, since competitive ETCs would generally have pricing flexibility, such
4 AUSF support should not be necessary.

5 11. *Should companies be required to file a rate case to obtain AUSF revenues?*

6 Not necessarily, although if rates are to be adjusted, certain information (including rate
7 base value) may be required. To the extent the AUSF would be used to compensate for serving
8 as a COLR in high-cost areas, the amount of support can be determined by comparing cost (as
9 determined by federal USF data, rather than through a rate case) to the corresponding revenue
10 amount. To the extent the AUSF would be used to replace revenues lost due to the elimination
11 of implicit subsidies, the applicable carrier would need to provide data demonstrating the loss of
12 revenue.

13 12. *If a rate case is not required, what method should be used to determine whether a*
14 *company should receive AUSF payments?*

15 To the extent the AUSF is to support the recovery of cost in high-cost areas, federal USF
16 data on loop and switching costs could be used to develop estimated costs related to supported
17 services. The resulting cost would then be compared to the corresponding federal benchmark;
18 any excess cost not already supported by federal law would be reimbursed by the AUSF.

19 Under a revenue replacement approach, the accepted methodology is for carriers to
20 compute a support payment based on the following calculation: [the reduction in access charge
21 per minute] multiplied by [the minutes of use in a previous base period, for example the year
22 preceding the change in access charge rules]. The base period minutes can be fixed at the time
23
24

1 of the access charge reduction, and based on volume before the reduction was made. The
2 support payment is typically paid in monthly installments.

3 13. *Should the AUSF rules be amended to allow for the provision of telephone service*
4 *in unserved or underserved areas?*

5 The AUSF rules currently allow for the provision of telephone service in unserved or
6 underserved areas. However, the AUSF does not provide additional support or incentives to a
7 carrier that expands service into these areas. To the extent that the AUSF is structured to provide
8 support for COLRs serving high-cost areas, as discussed above, it could appropriately provide
9 support for expansion into unserved or underserved areas, and the AUSF rules should be
10 amended to set forth the requirements for receiving support and the methodology for determining
11 the support amount, as noted in response to Question 6.

12 14. *Should the AUSF rules be amended to allow for incentives to companies to*
13 *provide telephone service in unserved or underserved areas?*

14 Yes, as described in response to Questions 6 and 13, the AUSF rules should be amended
15 so that the AUSF serves as a high-cost support fund. However, the AUSF should not provide a
16 one-time lump sum incentive to a carrier. The federal USF provides a mechanism for significant
17 cost recovery of expansion costs for most of the carriers in Arizona. If the Commission adopts a
18 high-cost support structure for the AUSF, carriers would have a mechanism to recover expansion
19 costs over the life of the asset which are not covered by the federal USF.

20 15. *Should the AUSF rules as proposed by ALECA be adopted?*

21 ALECA recognizes the need for access charge reform and should be commended for
22 seeking ways to achieve that reform. However, the Commission should not adopt ALECA's
23 proposal, as it is currently framed, for three reasons. First, ALECA does not suggest the removal
24 of common line cost recovery from access charges. Common line cost recovery is a form of

1 implicit subsidy,¹⁶ and the FCC has recognized that it is inappropriate to use a traffic sensitive
2 mechanism (the common line charge) to recover costs that are not traffic sensitive.¹⁷

3 Second, ALECA proposes adding the same flawed language that is currently found in the
4 Oklahoma rules (and that was recently removed from the Arkansas statutes and rules), which
5 allows a carrier to recover any decrease in federal USF support, even if the decrease is the result
6 of a decrease in the carrier's own revenue requirement or a revenue neutral rule change (which
7 by its nature would already be offset by revenues).

8 Third, the language in ALECA's proposed rule is unclear as to whether the carrier's
9 Interstate Common Line Support ("ICLS") would be considered in calculating support from the
10 state. It is important to include ICLS because the embedded loop costs developed by NECA
11 represent the total loop cost and the carrier's interstate loop cost recovery should be considered
12 in determining the level of intrastate support for loop cost.

13 16. *Should competitive bidding be a component of AUSF implementation?*

14 To the extent that the AUSF is intended to make explicit the universal service subsidies
15 implicit in intrastate access reform, there would be no place for a competitive process. However,
16 competitive processes may be worth considering for purposes of selecting a COLR, and
17 determining any necessary accompanying support, for area(s) where no existing carrier is ready,
18 willing or able to provide basic service. If the Commission is interested in pursuing such a
19

20 ¹⁶ *In re Multi-Association Group (MAG) Plan*, 16 F.C.C. Rcd. 19613, ¶ 15 (2001) ("We find that the
21 Carrier Common Line (CCL) charge, an inefficient cost recovery mechanism and implicit subsidy, should
be removed from the common line rate structure.").

22 ¹⁷ *Id.* at ¶ 17 ("The Commission has long recognized that, to the extent possible, interstate access costs
23 should be recovered in the manner in which they are incurred. In particular, non-traffic sensitive costs—
costs that do not vary with the amount of traffic carried over the facilities—should be recovered through
24 fixed, flat charges, and traffic sensitive costs should be recovered through per-minute charges. This
approach fosters competition and efficient pricing.") (footnote omitted).

1 procedure, it should solicit comments and/or hold workshops to explore the specific rules for
2 such competitive processes.

3 17. *Should CLECs have to prove a need for AUSF revenues?*

4 As previously discussed above, support should be limited to a single COLR. This would
5 preclude CLECs from receiving AUSF support (except, perhaps, for unserved areas where no
6 existing carrier is ready, willing, or able to provide basic service, and the Commission selects a
7 provider for such areas using competitive processes).

8 18. *What services should be eligible for inclusion in services supported by the AUSF?*

9 The basic level of services to be supported by the AUSF should generally mirror the
10 federal requirements found in 47 C.F.R. § 54.101(a)(1-9).

11 19. *Should AUSF payments be used for line extensions and if so how should eligible
12 costs be determined?*

13 *See Section II.A and response to Question 7 above.*

14 20. *How should the AUSF surcharges be calculated?*

15 As discussed above, to the extent that the FCC revises the federal USF contribution
16 methodology in the future, AT&T recommends that the Commission mirror the new federal
17 methodology at that time. In the meantime, the Commission should consider adopting an AUSF
18 contribution methodology more equitable than the one currently in place. The current 50/50
19 methodology may impose disproportionate burdens on certain categories of service providers.
20 AT&T currently anticipates providing a proposal for such a methodology in the next round of
21 comments.
22
23
24

1 21. *Should a program to improve participation in Lifeline and Link-up be supported*
2 *by AUSF?*

3 Yes. The Commission should review possible changes to the Lifeline program, including
4 the use of state funding to maximize the federal matching support and/or the level of
5 state-provided outreach.

6 22. *Should the enrollment program recommended by the ETCs be implemented or is*
7 *there another more cost effective method for increasing Lifeline and Link-Up*
8 *participation?*

9 The use of an automatic enrollment process, as proposed by the ETCs, could be a
10 reasonable means of increasing enrollment. However, the Commission may instead decide that
11 the use of a third-party administrator (similar to the approach used in Texas) would be a better
12 solution.

13 23. *Is the funding mechanism for the enrollment program recommended by the ETCs*
14 *appropriate, should the cost be borne by the ETCs as a cost of doing business and*
15 *being an ETC or is there some other method of funding that would be better?*

16 The use of AUSF funding to cover the costs of mechanizing enrollment is a reasonable
17 solution. The cost of Lifeline is not and should not be considered a "cost of doing business" for
18 carriers, but instead a form of subsidy that should be made explicit.

19 24. *Are the projections for potential Lifeline and Link-Up customers reasonable or is*
20 *there other data that would increase or decrease the cost/benefit estimates*
21 *contained in the ETC's Report? Please provide such data.*

22 The projections provided by ETC do not appear unreasonable on their face, but it is
23 difficult to know or project the impact of Lifeline program changes. The Commission should
24 consider alternative data sources, but AT&T does not have any data of its own.

25. *Should the recommendations in the ETC's Report be implemented, how should the AUSF rules be modified to address the enrollment program and the payments that would be made to the Department of Economic Security ("DES") for its participation?*

To the extent that the Commission decides to establish an automatic enrollment process, the rules necessary for such a process should be developed in a workshop setting that would allow the review and discussion of other states efforts at implementing a similar process.

26. *Should there be a “cap” on the payments that could be made to DES for its participation in the enrollment program and, if so, how might such a cap be determined?*

As stated in response to Question 22 above, the use of a third-party administrator might be preferred. Under that approach, the contract between the state and the third-party administrator would establish the amount of administrative expense ahead of time. The third party, not the state, would then bear the risk that costs might exceed the expected amount.

27. *Should there be some form of a “sunset clause” that would end the enrollment program and, if so, what would the appropriate criteria be for ending the program?*

No. The Commission should not establish an automatic sunset. Instead, the program should be reviewed every two to three years to determine if changes (including the elimination of automatic enrollment) should be made.

28. *To what extent do other states promote enrollment in Lifeline and Link-Up as recommended in the ETC's Report and to what extent have such state efforts been effective, both from an enrollment and cost perspective?*

The extent to which other states promote Lifeline and Link-Up varies from very limited to very extensive with varying levels of success. The suggestion, by the ETCs, to directly involve a state social services agency is not unprecedented, but more states are tending to opt for a third-party administrator. It is unusual to suggest that the Department of Revenue be involved.

1 The effectiveness of states' efforts and the cost benefits vary based on a number of factors, not
2 the least of which is local culture. In some areas, households would rather forego a phone, or
3 skip a meal or walk to save the cost of gas, rather than take a handout. In other areas, people
4 jump at discounted phone service. In other words, it is difficult to predict the success of a state's
5 efforts to promote Lifeline or to compare the effectiveness of one state's plan to another because
6 of the many cultural differences in the states.

7 29. *To what extent have communication services from the non-ETCs, such as prepaid*
8 *wireless offerings as one example, become the service of choice for eligible*
9 *Lifeline customers who otherwise may have subscribed to an ETC's Lifeline*
10 *service?*

11 AT&T does not have information sufficient to answer this question at this time.

12 RESPECTFULLY SUBMITTED this 7th day of January, 2008.

13 Isabelle Salgado
14 Gregory Castle
15 AT&T NEVADA
16 645 East Plumb Lane, B132
17 P.O. Box 11010
18 Reno, Nevada 89520

19 - and -

20 Demetrios G. Metropoulos
21 MAYER BROWN LLP
22 71 South Wacker Drive
23 Chicago, Illinois 60606
24

GALLAGHER & KENNEDY, P.A.

By Michael M. Grant

Michael M. Grant

2575 East Camelback Road

Phoenix, Arizona 85016-9225

Attorneys for AT&T Communications of the
Mountain States, Inc. and TCG Phoenix

Original and 15 copies filed this
7th day of January, 2008, with:

Docket Control

Arizona Corporation Commission

1200 West Washington Street

Phoenix, Arizona 85007

Copies of the foregoing mailed
this 7th day of January, 2008, to:

All parties who have filed requests
to remain on the service list

Dei Russell

17840-11/1745609